# Public Service Commission of Wisconsin



August 23, 1996



Office of the Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554

Re: In the Matter of Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996 — CC Docket No. 96-150

Gentlemen and Mesdames:

Pursuant to the Notice of Proposed Rulemaking, dated July 18, 1996, the Public Service Commission of Wisconsin is providing the enclosed comments. Enclosed are the original plus 11 copies as requested.

Sincerely,

Cheryl L. Parrino
Chairman

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Enclosure

cc: International Transcription Services, Inc.
Ernestine Creech, Common Carrier Bureau

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**Before the**
**FEDERAL COMMUNICATIONS COMMISSION**
**WASHINGTON, D.C. 20554**



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| Implementation of the | ) | |
| Telecommunications Act of 1996: | ) | CC Docket No. 96-150 |
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| Accounting Safeguards Under the | ) | |
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**COMMENTS OF THE**
**PUBLIC SERVICE COMMISSION OF WISCONSIN**

## SUMMARY

The Public Service Commission of Wisconsin (PSCW) appreciates the opportunity to file comments concerning accounting safeguards with the Federal Communications Commission (FCC). The PSCW advocates a cooperative relationship between federal and state regulators, not only in the area of accounting matters but in other aspects of implementation of the Telecommunications Act of 1996 (the 1996 Act), as well. The PSCW and commissions in other states have gained valuable experience in implementing competition in their respective jurisdictions. The FCC should draw on this experience to provide models that can be used to better achieve nationwide goals. Working together, the FCC and the states can accomplish the common goal of advancing competition, to the extent possible, in the telecommunications arena while providing certain protections and economies of scope benefits for telecommunications consumers.

The PSCW suggests the following concerning accounting safeguards:

1. The FCC does not possess the authority to preempt the states concerning intrastate accounting matters. Instead, FCC and state policies should coexist and be harmonized to promote telecommunications competition, detect cross-subsidies and protect and provide economies of scope benefits to telecommunications consumers. FCC policies should only be considered as a default when individual state actions become an obstacle to promoting such goals.

2. The PSCW supports the Notice of Proposed Rulemaking (NPRM) conclusion that the fully-allocated costing principles embodied in Section 32.27 and Part 64, as modified by the NPRM and the recommendations of the PSCW contained in these comments, meet the accounting and structural separation requirements of the 1996 Act. Part 32 and Part 64 rules should be further modified to clarify the definition of which costs can be included in regulated accounts. This is a result of the experience gained from the Ameritech Services, Inc., joint federal/state affiliated transactions audit.

3. The standard for separate employees specified in the 1996 Act, which is stricter than existing Section 32.27 or Part 64 rules, should only be applied to those subsidiaries where separation is required by the 1996 Act.

4. It is premature to conclude that the need for cost allocations has been eliminated for utilities under pure price cap regulation.

5. The PSCW suggests that the FCC consider the use of price floors to prevent cross-subsidization when developing its accounting principles governing affiliated transactions.

6. The FCC should use the audit guidelines and analysis contained in the resolution adopted July 25, 1996, by the National Association of Regulatory Utility Commissioners (NARUC) for the biennial audits required under § 272 of the Act. The audit guidelines and analysis should also, at a minimum, be used as a starting point for discussions concerning annual compliance reviews required under § 274 of the Act.

## PREEMPTION

**The Federal Communications Commission's interpretation of the Telecommunications Act of 1996 is in error with respect to its ability to prescribe regulations pertaining to intrastate activities. The FCC should utilize various states' experiences concerning implementation of competition to harmonize the federal and state policies and achieve a common goal: implementation of competition to the extent possible while protecting and providing economics of scope benefits to telecommunications consumers. Preemption should only be considered as a last resort in those instances where a state's policies become an obstacle to achieving this goal.**

In various paragraphs of the NPRM in CC Docket No. 96-150, the FCC tentatively concludes that it has jurisdiction over intrastate activities and, therefore, possesses the ability to prescribe intrastate cost allocation procedures and affiliated transaction rules.

The PSCW rejects the FCC's construction of the 1996 Act which purportedly grants the FCC jurisdiction over intrastate activities, including accounting matters, since the FCC's

analysis ignores § 601(c)(1) of the 1996 Act and nowhere else in the 1996 Act is the FCC explicitly granted jurisdiction over such accounting matters.

Section 601(c)(1) of the 1996 Act states as follows:

> (1) No implied effect. -- This Act and the amendments made by this Act shall not be construed to modify, impair, or supersede Federal, State, or local law unless expressly so provided in such Act or amendments.

The FCC relies on its analysis in the Notice of Proposed Rulemaking in CC Docket No. 96-149, in tentatively concluding it has jurisdiction over intrastate accounting matters. In its discussion in that notice, the FCC ignores the intent of § 2(b) of the Communications Act of 1934 (47 USC § 152(b)), which specifically reserves state jurisdiction over intrastate wire or radio communications. The limited exceptions noted in § 2(b) are not relevant to the FCC's leap of faith that § 251 of the 1996 Act somehow supersedes § 2(b). The notice in CC Docket No. 96-149, also argues that due to the 1996 Act's language concerning the AT&T Consent Decree (Modified Final Judgment), GTE Consent Decree and McCaw Consent Decree in § 601(a)(1) and §§ 271 and 272's language concerning LATAs, that the FCC has jurisdiction over intrastate activities for these two sections of the 1996 Act. The notice in CC Docket No. 96-150 extends this analogy to intrastate accounting matters concerning §§ 271 and 272, as well as to §§ 260 and 273 through 276, in varying degrees.

The manner in which Wisconsin is addressing issues concerning telecommunications competition is relevant to the discussion concerning preemption. The PSCW has adopted the FCC's Part 32 Uniform System of Accounts (USOA), with certain modifications.

Section 32.27 of the USOA was not adopted by the PSCW because of the existence of this Commission's long-standing affiliated interest statutory provision in s. 196.52 of the Wisconsin Statutes. Section 196.52, Wis. Stats., has for many years included the requirement that affiliated interest agreements be reduced to writing for public inspection. The 1996 Act recently added that requirement on a national basis. In addition, while not having formally adopted Part 64 of the FCC's rules, the PSCW has used it for intrastate revenue requirement and earnings monitoring calculations. The Wisconsin Statutes also define an imputation test in ss. 196.204(5) and (6), Wis. Stats., and address protection of telecommunications consumers in s. 196.219, Wis. Stats. A copy of the above-referenced sections of the Wisconsin Statutes are contained in Appendix A. There has long been a successful interplay of federal and state rules in all of these areas.

Nothing in the Wisconsin Statutes nor in the PSCW procedures would frustrate the accomplishment of the goals espoused in the 1996 Act. Therefore, the FCC can not preempt intrastate activities, including accounting matters, on this basis.

Instead of a preemptive approach, the PSCW supports the coexistence and harmonization of FCC and state policies concerning promotion of telecommunications competition, while at the same time facilitating the detection of cross-subsidies and the protection of and provision of economies of scope benefits to telecommunications consumers. The FCC's policies should only be considered as a default when individual state actions do not accomplish these goals.

## MODIFICATION OF PART 32 AND PART 64 RULES

**The PSCW supports the NPRM conclusion that the principles of Section 32.27 and Part 64, as modified by the NPRM and the PSCW's suggested comments, meet the accounting and structural separation requirements of the 1996 Act. Based on the experience of the Ameritech Services, Inc., federal/state joint audit, Part 32 and Part 64 rules should be further modified to clarify the definition of which costs can be included in regulated accounts.**

The FCC's proposed modifications to Section 32.27 are reasonable. The PSCW has previously supported these changes in its comments filed in CC Docket No. 93-251. The proposed modifications restate the LOCOM/HOCOM[1] standard, and impose a limitation on the use of prevailing market price when a small portion of business transactions are conducted with unaffiliated third parties. The current NPRM further clarifies other proposals. It clarifies that valuation methods apply to both services and assets. The NPRM raises a concern whether wholesale discounts should apply when large volumes of transactions occur with affiliates. It includes proposed criteria for determining when a good faith estimate of fair market value should be made.

In our comments in CC Docket No. 93-251, the PSCW expressed a concern regarding the valuation of a transaction when assets which have been previously expensed by a utility are later transferred to an affiliate. Utilities have claimed such assets have no value in recording the transfer. The clarification in the NPRM that valuation methods apply to both services and assets, in part, addresses this concern. In addition, the proposed criterion of

[1] Lower of Cost or Market (LOCOM) / Higher of Cost or Market (HOCOM).

requiring a fair market value determination when the transaction is subject to reasonable independent valuation methods addresses this issue. The NPRM further requires the use of methods and principles similar to those that would be used by an independent appraiser when it is difficult to obtain an independent appraisal. These further modifications proposed in this NPRM address the concerns from the PSCW's comments previously filed.

The PSCW proposes an additional modification to the Part 32 and Part 64 rules based upon our experience in the federal/state joint affiliated transactions audit of Ameritech Services, Inc. (ASI), conducted by PSCW personnel with staff of the Public Utilities Commission of Ohio and the FCC. As a result of that audit, the FCC issued a Consent Decree Order in Docket AAD 95-75. Ameritech agreed, pursuant to the consent decree, that it would maintain the necessary records to justify recording costs to, or allocations of costs to regulated accounts. In light of Ameritech's reply to the audit finding as quoted below, modification of the Part 32 and Part 64 rules appears necessary to codify this requirement for all telecommunications utilities and provide a standard for the anticipated biennial audits and annual compliance reviews to be carried out under the 1996 Act.

> The audit team fails to articulate the Part 32 or Part 64 rule which requires the [operating company] to demonstrate that the services provided from ASI were beneficial to the [operating company]. In this regard, neither Part 32 nor Part 64 of the Commission's rules establish any standard by which to make a qualitative or quantitative evaluation of the products and services provided by affiliates. Rather,

> Part 32 and Part 64 rules require the proper recording and accounting of regulated and nonregulated costs. The rules do not address whether those costs are reasonable.[2]

In the consent decree, Ameritech agreed to maintain documentation of the benefit to the operating company resulting from transactions with ASI. It agreed to maintain the following documentation.

> These forms will indicate the benefit of the activity to [operating company] regulated services and will include a signed statement from the appropriate [operating company] confirming the benefit or benefits to that [operating company] as listed therein. In addition to information required by other ASI procedures, the benefit should include, as appropriate, an analysis of (1) potential revenue losses or future costs if the project is not undertaken compared to costs expected to be incurred; (2) additional regulated revenues expected to be generated compared to costs incurred; (3) improvement in the quality of regulated services; (4) other benefits; or (5) a statement explaining why none of the above was included.

The abuse these requirements address is the potential for a subsidiary to engage in work that primarily benefits its nonregulated activity while it charges regulated accounts for the costs of the work. Codification in Part 32 and Part 64 of the documentation that is necessary to record amounts to regulated accounts will assist in setting the objectives of affiliated transactions audits to independent auditors who will be hired to perform the biennial audits and annual compliance reviews required by the 1996 Act.

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[2] Ameritech's Response to the Report of the Joint Audit Team's Review of Affiliate Transactions at Ameritech Services, Inc., May 1995, page 17.

## SHARING OF EMPLOYEES

**The standard for separate employees specified in the 1996 Act should only be applied to those subsidiaries where separation is required by the 1996 Act.**

The existing Section 32.27 rules are designed so as to achieve the maximum degree of economies of scale and scope while providing sufficient protection. Nothing in those rules or the Part 64 rules requires separate employees. We present the following interpretation of the stricter requirement contained in the 1996 Act. We believe the requirement for separate employees should apply only to the limited number of affiliates which are required to use structural safeguards under the 1996 Act for a limited time period. Separate employees provide an added degree of protection at an added cost as the potential damage to competition caused by cross-subsidies is so great when markets are initially opened to competition.

For the circumstances where optional separate affiliates are used, or the 1996 Act provision sunsets, the affiliates should be able to achieve economies of scale and scope. This would argue for sharing of employees in these circumstances. The separate employee requirement could be codified in a unique section of the affiliated interest rules so that it applies only to situations identified in the 1996 Act. For those companies that utilize an optional separate affiliate, or when the 1996 Act's requirements for affiliates sunset, then that section of the rules would no longer apply. This would carry out the requirement of the 1996 Act, but only sacrifice economies of scale and scope to the extent that added protection, and associated costs, of separate affiliates are required.

## PURPOSE OF COST ALLOCATIONS

**It is premature to conclude that the need for cost allocations, fully allocated or otherwise, has been eliminated for utilities under pure price cap regulation.**

The NPRM asks the question whether pure price cap regulation with no sharing mechanism eliminates the need for cost allocations. In response, the PSCW believes it is premature to arrive at such a conclusion when the definitions for subsidy and cross-subsidy have not been clearly delineated. Multiple interpretations of the term, "subsidy," are possible. Some would argue that the antitrust definition of subsidy should be used in the enforcement of these statutes. On the other hand, cost allocations resulting from Part 32 and Part 64 of the FCC rules are based upon fully-allocated costs.

Wisconsin statutes include regulatory responsibilities to limit or prevent telephone exchange services from providing subsidies to other services. In 1993 Wisconsin Act 496, a balancing of the interests of local exchange carriers, interexchange carriers and other new entrants resulted in the inclusion of s. 196.204, Wis. Stats., titled, "Cross-subsidization limited." The PSCW currently has pending a proceeding, docket 1-AC-163, for establishing cross-subsidy rules. Since the passage of 1993 Wisconsin Act 496, there has not been any case before the PSCW which interpreted the meaning of subsidy. Therefore, the precise valuation method(s) required by the phrase, "may not subsidize," contained in s. 196.204(1), Wis. Stats., remains unclear at this time.

Federal statutes also include regulatory responsibilities to limit or prevent telephone exchange access services from providing subsidies to other services. In §§ 260 and 271

through 276 of the 1996 Act, language repeatedly requires that new services shall not be subsidized directly or indirectly by telephone exchange access. However, no statutory definition is given for subsidy. Numerous joint cost orders have preceded the 1996 Act. The 1996 Act refers to accounting safeguards at least equal to those adopted in the Computer Inquiry III for § 276(b)(1)(c), Provision of Payphone Service. The FCC's recent order in CC Docket No. 96-98 sets forth a requirement for an allocation of forward-looking common costs in determining the pricing of interconnection and unbundled elements. This requirement provides some evidence that the intent of the "shall not subsidize" language includes a sharing of common costs.

While cost allocations may not affect prices of telephone exchange access service for pure price cap utilities, the allocated costs will appear on the books of structurally separate affiliates as federal statutes repeatedly require that separate affiliates maintain separate books, records and accounts. It would be unwise to forego this basic information before state commissions even begin to carry out their regulatory responsibilities related to cross-subsidization. Accordingly, it is premature to consider the elimination of cost allocation requirements.

## WISCONSIN IMPUTATION TEST

**The PSCW suggests that the FCC consider, when it develops its accounting principles as required by § 272(c)(2), the use of price floors to prevent cross-subsidization.**

At this time, the PSCW also would like to take the opportunity to describe the price floors that exist in Wisconsin to prevent cross-subsidies. We will summarize earlier comments sent to the FCC in CC Docket No. 95-20 which discuss the importance of price floors.

Wisconsin cross-subsidy statutes contain a clearly defined imputation test in ss. 196.204(5) and (6), Wis. Stats. That imputation test must be met when any utility or its affiliate[3] uses a noncompetitive service in the provision of its own competitive service. Paraphrasing, it requires that the telecommunications service be priced to exceed total service long-run incremental cost (TSLRIC), as defined in s. 196.015, Wis. Stats., with a waiver possible for basic local service.[4] By applying a price floor in this manner, competitors are protected from price squeezes.

The PSCW described this price floor in its comments previously submitted in CC Docket No. 95-20, Computer III Further Remand. Those comments explained that under price cap regulation accounting safeguards are less effective than under rate base rate-of-return

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[3] In Wisconsin, affiliates, certified as Alternative Telecommunications Utilities (ATUs), if made subject to section 196.204, would be treated as a utility for purposes of imputation.

[4] To date, there has not been any case before the PSCW which interpreted the meaning of TSLRIC.

regulation when periodically rates were adjusted based on accounting costs. Under a form of price cap regulation, it is acknowledged that at times efficiencies and innovations can lead to earnings which are above-normal returns. Protection is needed to prevent such above-market returns from funding market-contracting strategies. Price floors like the Wisconsin imputation test provide that protection.

Accordingly, we suggest that the FCC consider, when it develops its accounting principles as required by § 272(c)(2) of the 1996 Act, the use of price floors to prevent cross-subsidization.

## REQUIRED AUDITS UNDER § 272 AND COMPLIANCE REVIEWS UNDER § 274

**The FCC should utilize the audit guidelines and analysis contained in the resolution adopted July 25, 1996, by NARUC for the biennial audits required under § 272 of the 1996 Act. The audit guidelines and analysis should also, at a minimum, be used as a starting point for discussions concerning annual compliance reviews required under § 274 of the 1996 Act.**

Section 272 of the 1996 Act requires that a biennial audit be conducted by an independent auditor covering transactions between a Bell operating company and its affiliates engaged in manufacturing activities, origination of interLATA telecommunications services, and interLATA information services. The NARUC, of which the PSCW is a member, recently passed a resolution concerning § 272 audits. The PSCW supports the positions expressed in the resolution and recommends that the FCC adopt these guidelines and analysis for the § 272 audits. A copy of this resolution is attached as Appendix B.

Section 274 of the 1996 Act requires electronic publishing separated affiliates or joint ventures and the Bell operating company with which it is affiliated to have an annual compliance review performed. While the NARUC resolution was tailored to the § 272 biennial audits and did not expressly address the § 274 annual compliance reviews, the PSCW would recommend that the FCC use the NARUC resolution as a starting point for discussions between the states and the FCC concerning such reviews.

**CONCLUSION**

The PSCW believes that a cooperative approach to implementation of the 1996 Act is the best policy for all concerned. This is especially true with respect to accounting matters. The PSCW has suggested several improvements to the FCC's Part 32 and Part 64 rules which it believes will be beneficial to the development of competition, detection of cross-subsidies, and protection of and provision of economies of scope benefits to telecommunications consumers.

Please consider these comments in rendering your decision in this proceeding.

Respectfully Submitted,

Cheryl L. Parrino
Chairman

August 23, 1996

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Attachments

## APPENDIX A

WISCONSIN STATUTORY REFERENCES

**Section 196.204 Cross-subsidization limited. (referenced in sections 196.219 and 196.52)**

**196.204 Cross-subsidization limited.** **(1)**Except for retained earnings, a telecommunications utility may not subsidize, directly or indirectly, any activity, including any activity of an affiliate, which is not subject to this chapter or is subject to this chapter under s. 196.194, 196.195, 196.202 or 196.203. [nonrelevant material] No telecommunications utility may allocate any costs or expenses in a manner which would subsidize any activity which is not subject to this chapter or is subject to this chapter under s. 196.194, 196.195, 196.202 or 196.203. [nonrelevant material] Except as provided in subs. (2) and (4) the commission may not allocate any revenue or expense so that a portion of a telecommunications utility's business which is fully regulated under this chapter is subsidized by any activity which is not regulated under this chapter or is partially deregulated under s. 196.194, 196.195, 196.202 or 196.203. [nonrelevant material]
**(2)** The commission may attribute revenues derived from the sale of directory advertising or directory publishing rights to the regulated activities of a telecommunications utility for rate making and other utility purposes.

...

**(4)** In order to protect the public interest, the commission may allocate the earnings derived from sale of services partially deregulated under s. 196.195, 196.202 or 196.203 [nonrelevant material] to the fully regulated activities of a telecommunications utility for rate-making purposes.
**(5)** (a) In addition to the other requirements of this section, each telecommunications service, relevant group of services and basic network function offered or used by a telecommunications utility shall be priced to exceed its total service long-run incremental cost. The commission may waive the applicability of this paragraph to a telecommunications utility's basic local exchange service if the commission determines that a waiver is consistent with the factors under s. 196.03 (6).

...

**(6)** (a) In addition to the other requirements of this section, a telecommunications utility shall meet the imputation test in this subsection if all of the following apply:

1. The telecommunications utility has a service offering that competes with an offering of another telecommunications provider.

2. The other telecommunications provider's offering utilizes a service, including any unbundled service element or basic network function, from the telecommunications utility that is not available within the relevant market or geographic area on reasonably comparable terms and conditions from any other telecommunications provider.

3. The telecommunications utility's own offering uses that same noncompetitive service, or its functional equivalent.

(b) The price of a telecommunications service subject to an imputation test shall exceed the sum of all of the following:

1. The tariffed rates, including access, carrier common line, residual interconnection and similar charges, for the noncompetitive service or its functional equivalent that is actually used by the telecommunications utility in its service offering, as those rates would be charged any customer for the use of that service.

2. The total service long-run incremental costs of all other components of the telecommunications utility's service offering, including access charges actually paid.

...

**(Emphasis added.)**

**Section 196.015 Total service long-run incremental cost. (Section 196.015 contains the definition of total service long-run incremental cost, which is referenced in section 196.204(5)(a))**

**196.015 Total service long-run incremental cost. (1)** In this section, "basic network function" means the smallest disaggregation of local exchange transport, switching and loop functions that is capable of being separately listed in a tariff and offered for sale.

**(2)** In this chapter, total service long-run incremental cost is calculated as the total forward-looking cost, using least cost technology that is reasonably implementable based on currently available technology, of a telecommunications service, relevant group of services, or basic network function that would be avoided if the telecommunications provider had never offered the service, group of services, or basic network function or, alternatively, the total cost that the telecommunications provider would incur if it were to initially offer the service, group of services, or basic network function for the entire current demand, given that the telecommunications provider already produces all of its other services.

**Section 196.03 Utility charges and service; reasonable and adequate. (Section 196.03(6) is referenced in sections 196.204(5)(a) and 196.219)**

...

**(6)** In determining a reasonably adequate telecommunications service or a reasonable and just charge for that telecommunications service, the commission shall consider at least the following factors in determining what is reasonable and just, reasonably adequate, convenient and necessary or in the public interest:

(a) Promotion and preservation of competition consistent with ch. 133 [nonrelevant material] and s. 196.219.

(b) Promotion of consumer choice.

(c) Impact on the quality of life for the public, including privacy considerations.

(d) Promotion of universal service.

(e) Promotion of economic development, including telecommunications infrastructure deployment.

(f) Promotion of efficiency and productivity.

(g) Promotion of telecommunications services in geographical areas with diverse income or racial populations.

**Section 196.52 Relations with affiliated interests; definition; contracts with affiliates filed and subject to commission control.**

...

**(3)** (a) In this subsection, "contract or arrangement" means a contract or arrangement providing for the furnishing of management, supervisory, construction, engineering, accounting, legal, financial or similar services and any contract or arrangement for the purchase, sale, lease or exchange of any property, right, or thing, or for the furnishing of any service, property, right, or thing, other than management, supervisory, construction, engineering, accounting, legal, financial or similar services. Except as provided under par. (b), unless and until the commission gives its written approval, any contract or arrangement is not valid or effective if the contract or arrangement is made between a public utility and an affiliated interest after June 7, 1931. Every public utility shall file with the commission a verified copy of any contract or arrangement, a verified summary of any unwritten contract or arrangement, and any contract or arrangement, written or unwritten, which was in effect on June 7, 1931. The commission shall approve a contract or arrangement made or entered into after June 7, 1931, only if it shall clearly appear and be established upon investigation that it is reasonable and consistent with the public interest. The commission may not approve any contract or arrangement unless satisfactory proof is submitted to the commission of the cost to the affiliated interest of rendering the services or of furnishing the property or service to each public utility

or of the cost to the public utility of rendering the services or of furnishing the property or service to each affiliated interest. No proof is satisfactory under this paragraph unless it includes the original (or verified copies) of the relevant cost records and other relevant accounts of the affiliated interest, or an abstract of the records and accounts or a summary taken from the records and accounts if the commission deems the abstract or summary adequate. The accounts shall be properly identified and duly authenticated. The commission, where reasonable, may approve or disapprove a contract or arrangement without submission of the cost records or accounts.

(b) 1. The requirement for written approval under par. (a) shall not apply to any contract or arrangement if the amount of consideration involved is not in excess of $25,000 or 5% of the equity of the public utility, whichever is smaller, and does not apply to a telecommunications utility contract or arrangement. Regularly recurring payments under a general or continuing arrangement which aggregate a greater annual amount may not be broken down into a series of transactions to come within the exemption under this paragraph. Any transaction exempted under this paragraph shall be valid or effective without commission approval under this section.

2. In any proceeding involving the rates or practices of the public utility, the commission may exclude from the accounts of the public utility any payment or compensation made pursuant to a transaction exempted under this paragraph unless the public utility establishes the reasonableness of the payment or compensation.

(c) If the value of a contract or arrangement between an affiliated interest and a public utility, other than a telecommunications utility, exceeds $1,000,000, the commission:

1. May not waive the requirement of the submission of cost records or accounts under par. (a);

2. Shall review the accounts of the affiliated interest as they relate to the contract or arrangement prior to the commission approving or disapproving the contract or arrangement under par. (a); and

3. May determine the extent of cost records and accounts which it deems adequate to meet the requirements for submission and review under subds. 1 and 2.

...

5. (b) For telecommunications utilities, the commission shall have supervisory jurisdiction over the terms and conditions of contracts and arrangements under this section as necessary to enforce ss. 196.204 and 196.219.

**(Emphasis added.)**

**Section 196.219 Protection of telecommunications consumers. (referenced in section 196.52)**

**196.219 Protection of telecommunications consumers.**

**(1)** DEFINITION. In this section, "consumer" means any person, including a telecommunications provider, that uses the services, products or facilities provided by a telecommunications utility.

**(2)** CONSUMER PROTECTION. (a) Notwithstanding any exemptions identified in this chapter except s. 196.202, [nonrelevant material] a telecommunications utility shall provide protection to its consumers under this section unless exempted in whole or in part by rule or order of the commission under this section. The commission shall promulgate rules that identify the conditions under which provisions of this section may be suspended.

(b) On petition, the commission may grant an exemption from a requirement under this section upon a showing that the exemption is reasonable and not in conflict with the factors under s. 196.03 (6).

(c) On petition, the commission may grant an exemption from a requirement under this section retroactively if the application of the requirement would be unjust and unreasonable considering the factors under s. 196.03 (6) or other relevant factors.

(d) If the commission grants an exemption under this subsection, it may require the telecommunications utility to comply with any condition necessary to protect the public interest.

**(2m)** ACCESS SERVICES. (a) A telecommunications utility shall provide access services under tariff under the same rates, terms and conditions to all telecommunications providers.

(b) Paragraph (a) does not apply to cellular telephone interconnection arrangements authorized or required by the federal communications commission.

**(3)** PROHIBITED PRACTICES. A telecommunications utility may not do any of the following with respect to regulated services:

(a) Refuse to interconnect within a reasonable time with another person to the same extent that the federal communications commission requires the telecommunications utility to interconnect. The public service commission may require additional interconnection based on a determination, following notice and opportunity for hearing, that additional interconnection is in the public interest and is consistent with the factors under s. 196.03 (6).

(b) Upon request, fail to disclose in a timely and uniform manner information necessary for the design of equipment and services that will meet the specifications for interconnection.

(c) Impair the speed, quality or efficiency of services, products or facilities offered to a consumer under a tariff, contract or price list.

(d) Unreasonably refuse, restrict or delay access by any person to a telecommunications emergency service.

(e) Fail to provide a service, product or facility to a consumer other than a telecommunications provider in accord with the telecommunications utility's applicable tariffs, price lists or contracts and with the commission's rules and orders.

(em) Refuse to provide a service, product or facility to a telecommunications provider in accord with the telecommunications utility's applicable tariffs, price lists or contracts and with the commission's rules and orders.

(f) Refuse to provide basic local exchange service, business access line and usage service within a local calling area and access service on an unbundled basis to the same extent that the federal communications commission requires the telecommunications utility to unbundle the same services provided under its jurisdiction. The public service commission may require additional unbundling of intrastate telecommunications services based on a determination, following notice and opportunity for hearing, that additional unbundling is required in the public interest and is consistent with the factors under s. 196.03 (6). The public service commission may order unbundling by a small telecommunications utility.

(g) Provide services, products or facilities in violation of s. 196.204.

(h) To the extent prohibited by the federal communications commission, or by the public service commission under rules promulgated consistent with the factors under s. 196.03 (6), give preference or discriminate in the provision of services, products or facilities to an affiliate, or to the telecommunications utility's own or an affiliate's retail department that sells to consumers.

(j) Restrict resale or sharing of services, products or facilities, except for basic local exchange service other than extended community calling, unless the commission orders the restriction to be lifted. A telecommunications utility that has 150,000 or less access lines in use in this state may limit the use of extended community calling or business line and usage service within a local calling area as a substitute for access service, unless the commission orders the limitation to be lifted.

(L) Fail to provide, or to terminate, any telecommunications service as necessary to comply with the minimum standards of service established by the commission with respect to technical service quality, deposits, disconnection, billing and collection of amounts owed for services provided or to be provided.

(m) Provide telecommunications service to any person acting as a telecommunications utility, telecommunications provider, alternative telecommunications utility or telecommunications carrier if the commission has ordered the telecommunications utility to discontinue service to that person.

(n) Provide telecommunications service in violation of s. 100.207. [nonrelevant material]

**(4)** ENFORCEMENT. (a) On the commission's own motion or upon complaint filed by the consumer, the commission shall have jurisdiction to take administrative action or to commence civil actions against telecommunications utilities to enforce this section.

(b) The commission may, at its discretion, institute in any court of competent jurisdiction a proceeding against a telecommunications utility for injunctive relief to compel compliance with this section, to compel the accounting and refund of any

moneys collected in violation of this section or for any other relief permitted under this chapter.

**(4d)** UNFAIR TRADE PRACTICE ENFORCEMENT. Upon receipt of a notice issued under s. 100.208, [nonrelevant material] the commission may order a telecommunications provider to cease offering the telecommunications service that creates the unfair trade practice or method of competition.

**(4m)** CIVIL ACTIONS. Upon a finding of a violation of this section by the commission, any person injured because of a violation of this section by a telecommunications utility may commence a civil action to recover damages or to obtain injunctive relief.

**(5)** ALTERNATE DISPUTE RESOLUTION. The commission shall establish by rule a procedure for alternative dispute resolution to be available for complaints filed against a telecommunications utility.

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**(Resolution as shown on pages 5 through 9 of the National Association of Regulatory Utility Commissioners bulletin, NARUC No. 32-1996, dated August 5, 1996)**

**Resolution to Support the Attached Audit Guidelines and Analysis to Comply with the Current Federal Legislation to Prevent Cross Subsidization**

**WHEREAS**, The Federal Communications Commission (FCC) and the National Association of Regulatory Utility Commissioners (NARUC) have participated in successful joint audits; and

**WHEREAS**, The FCC and State staffs have benefited from the joint audits and developed professional expertise that has been shared among the regulatory staff nationally, and high quality guidelines for past audits have been developed; and

**WHEREAS**, The "Telecommunications Act of 1996" (this Act) will require new audit guidelines and a joint audit approach to the implementation of this Act would be an economical and efficient means to achieve the intent of this Act; and

**WHEREAS**, This Act requires that the Bell Operating Companies pay for biennial joint Federal/State audits by independent auditors to ensure that the companies meet the separate affiliate requirements of Section 272 and that those audits be made available to the FCC and appropriate state commissions; and

**WHEREAS**, The Executive Committee of NARUC, convened at its 1996 Winter Meeting in Washington, D.C., authorized the Subcommittees on Communications and Accounts to perform or cause to perform.

joint audits with the FCC in a comprehensive manner in the areas of cost of current regulated services, the cost of spare capacity and the transfer of resources to the new non-regulated services and also work cooperatively to ensure that the audits are performed in compliance with Section 272 of the Act; and

**WHEREAS**, On February 28, 1996, The NARUC Executive Committee adopted a resolution, jointly sponsored by the Committees on Communications and Finance and Technology, which stated that in keeping with the spirit of cooperation set forth in the NARUC Executive Committee Resolutions adopted 2-28-90 and 11-13-91 regarding joint or coordinated FCC and State Audits and the potential benefits derived from such audits, the Subcommittees were directed to invite and work with the FCC staff to prepare uniform joint audit guidelines under the "Telecommunications Act of 1996, to be presented as a proposal to the respective parent committees at the NARUC Summer meetings in Los Angeles, California; and

**WHEREAS**, The Staff Subcommittees on Communications and Accounts, through the Federal/State RBOC Joint Audit Oversight Committee, have developed audit guidelines; now, therefore, be it

**RESOLVED**, That the Executive Committee of the National Association of Regulatory Utility Commissioners (NARUC), convened at its 1996 Summer Meeting in Los Angeles, California, adopts the attached audit guidelines and analysis regarding the implementation of Section 272 of the Telecommunications Act of 1996 as prepared by the state members of the Joint Federal/State RBOC Staff Audit Oversight Committee; and be it further

**RESOLVED**, That a separate joint federal/state audit team, consisting of staff members from federal and state regulatory commissions, should be set up, consistent with state and federal law, to monitor and oversee the audit processes required by the Telecommunications Act of 1996, especially compliance with Section 272 of the Act.

Sponsored by the Committees on Communications and Finance and Technology

Adopted July 25, 1996

**I. INTRODUCTION**

Under a Resolution sponsored jointly by the Committees on Communications and Finance and Technology and adopted on February 28, 1996, the Subcommittee on Communications and the Subcommittee on Accounts were directed to invite and work with the Federal Communications Commission (FCC) and staff to prepare uniform joint audit guidelines under the "Telecommunications Act of 1996." In this document, we are seeking to carry out our directive and clarify and present our interpretation of several points throughout Section 272. Separate Affiliate; Safeguards while attempting to outline the role of the State commissions and the FCC in the audit process. In Section 272(d)(1), it is stated that "a company required to operate a separate affiliate under this section shall obtain and pay for a joint Federal/State audit...". In addition, there are several specific guidelines, requirements and responsibilities included in the Section. Our goal here is to address the most appropriate and efficient execution of those guidelines and responsibilities.

**II. FEDERAL AND STATE ROLE**

First, we believe a separate joint Federal/State audit team (the Team) should be set up to monitor and oversee the audit process. A team consisting of Federal and State regulators should be formed to oversee and monitor the audit process as it relates to compliance with Section 272. The Team members should be appointed by the NARUC Subcommittee on Communications and the Subcommittee on Accounts. In many instances in the text of Section 272, State and Federal action is mentioned. Where possible, the Team should have the responsibility of completing those actions.

The Team should have access to a staff of auditors who will be assigned to the audits and who will be directly responsible for monitoring the steps in the audit process. The Team audit staff should consist of members of Federal and State regulatory commissions. The State commissions in which a particular company operates would have the first opportunity to volunteer members of their staff to serve on the Team audit staff. All States should have the right to join the team or participate on an individual State basis. An alternative would be to establish a joint board for this purpose.

The Team should not be a party to the contract between the company and the auditor. The Section stated that the audit should be obtained and paid for by the company. Therefore, only the company and the auditor should be party to the contract. However, this does not preclude the team from being involved in determination of the scope of the audit and review of the audit.

Companies should be required to use Requests For Proposals (RFP) to choose auditors to complete the audits required by Section 272. The RFP process will benefit the ratepayers by creating a more competitive decision process while still allowing the companies to choose their own auditors to complete the required audits.

An RFP should include:

· The purpose and the scope of the audit, i.e., to verify compliance with structural and transitional separation requirements as well as anti-discrimination requirements, etc., as required in Section 272;

· A provision for disclosure of the nature and timing of any recent work done for the company or any of its affiliates. Depending upon the type of services performed, the auditor should not be considered for selection in this audit engagement. For example, if the bidder or his/her affiliate was instrumental in designing any of the systems that will be under review in the audit, there may be a conflict of interest in retaining that firm to provide the audit services.

· Auditor selection criteria, with emphasis on the proposed work plan and previous experience of proposed personnel in evaluating affiliate relationships/cost allocations in the telecommunications industry;

· Project controls, including progress reports and a work paper trail with respect to interviews conducted, data collected, auditor analysis, etc.;

· Content of the draft and final reports with requirements for prioritization and quantification of recommendations;

· Provision of company written comments to both the draft and final reports; and

· Provision for protection of proprietary data, by the selected auditor, for which they may have access to during the audit.

· Upon completion of an audit, provision for retention of all workpapers on company premises or guaranteed access to workpapers if they remain in the auditor's custody.

The Team should become involved in the audit process before the auditor is chosen. The Team should develop a set of standards or objectives which must be met in all audits. These audit standards or objectives should be developed to compliment those that may be established by the FCC. In turn, these standards and objectives should be incorporated into the RFP. We recommend that the Team become involved at this level so that when an auditor is chosen, that auditor is very much aware of the responsibilities involved in completing the audit. Knowing what is expected from all involved will help facilitate cooperation between the independent auditor and the Team.

The Team should obtain and perform a brief review of the RFP and contract prior to company proposal solicitation. The objective of this review would be to determine if the documents generally meet the guidelines set out above. After tentative selection of a proposal by the company, the Team should obtain and briefly review that proposal for general conformance to the RFP requirements with an emphasis on the proposed work plan and audit techniques to be used.

A designated Team audit staff member should be assigned to be responsible for following the progress of the audit and to act as liaison between the Team, the auditor and the company. This individual should handle all correspondence between the Team and the auditor or company. The individual will also have the responsibility for monitoring whether deadlines will be met and whether objectives are being met. There may be, however, depending on the size of an audit, more than one auditor assigned to follow and monitor an audit.

Specific areas of Team involvement during the audit should be as follows:

· The company should notify the Team of the start of the audit. The assigned members of the Team audit staff should be in attendance at the kick-off meeting to gain an overall perspective on how the project is to be carried out in the field and the administrative procedures established to control it.

· The company or the independent auditor should forward any detailed or revised work plans to the Team audit staff for review and comments, if any.

· The company should forward all periodic progress reports prepared by the auditor to the audit staff for review and comments, if any.

· The company should forward draft report(s) and any company written comments to the Team audit staff for their review and comments. Also, changes to the draft should be supported by written comments from the companies.

· The Team audit staff assigned should obtain and review audit work papers as necessary to determine if they meet professional standards and provide adequate support for findings and conclusions reached by the auditor.

· The Team audit staff should have the option of attending and therefore receive notice ofany meetings held between the auditor and the company where audit procedures or findings are discussed.

Upon completion of the audit, but prior to issuance of the independent auditor's opinion as to compliance with Section 272, the Team should verify that the program objectives were met. An additional benefit of utilizing the RFP process will be that the auditor is contractually obligated to fulfill all scope requirements, therefore, it will be more likely that the specified items will be completed. However, if all were not met, or if the Team determined that additional inquiry is necessary, the auditor should be required to meet the objectives and make the additional inquiry or be required to show why it cannot. The Team should be able to issue a Team comment, if the Team so desires, regarding the audit process.

The final non-proprietary report and company response, including plans to implement any recommendations, should be submitted to the Team for dissemination to the FCC and the appropriate State commissions. In addition, only the non-proprietary report should be made public to interested parties, with copies provided. Finally, the company should submit an implementation progress report to the Team audit staff approximately six months prior to the next audit. To help improve the effectiveness and efficiency of future audits, the Team should consider how the final report, the interested party comments and the implementation progress report impact the scope of the next audit.

## III. AREAS OF GENERAL CLARIFICATION AND INTERPRETATION

Point of Clarification and Interpretation/Recommendation

How should the audit fees be accounted for?

The expenses associated with the audits should be recorded on the books of the affiliates on which the audit is being performed.

What does the phrase "shall maintain books, records, and accounts in the manner prescribed by the Commission" mean as stated in Section 272(b)(2)? Should the FCC issue specific requirements for the recordkeeping of books and records by the affiliate?

In order to facilitate more timely and accurate analysis of company records and activities, the affiliated company should be required to follow the same system of accounts as the companies which are subject to Section 272 or be able to provide the independent auditor and the Team audit staff with a document which cross-references the accounts of the company with those of the affiliate. The records of both the company and the affiliate should be readily comparable to facilitate review.

How is the auditor to assure compliance with the separate accounting requirements in Section 272(b)?

Operation requirements for the affiliate are stated in Section 272(b). In order to assure compliance, the auditor must plan and perform the audit to provide him or herself with a sufficient level of knowledge to determine:

· whether the affiliate has maintained separate books, records, and accounts than those of the company;

· whether the affiliate has separate officers and directors, and that no employees are shared by the affiliate and the company;

· what sort of financing the affiliate has obtained and the type and ownership of the affiliates stock; and

· the nature and amounts for any transactions between the affiliate and the company.

Should Team members, Team audit staff members or other commission staff members be reimbursed for travel expense incurred in connection with the requirements of Section272?

The companies should reimburse Team members, Team audit staff members and Federal and State commission staff members for reasonable travel expenses that are